No. 13,156

IN THE

United States Court of Appeals

For the Ninth Circuit

STERLING CARR, Trustee of the Estate of Nippon Yusen Kaisya, a corporation, bankrupt,

Appellant,

vs.

THE YOKOHAMA SPECIE BANK, LTD., OF SAN FRANCISCO, a foreign corporation, and MAURICE C. SPARLING, as Superintendent of Banks of the State of California and Liquidator of the Yokohama Specie Bank, Ltd., San Francisco Office,

Appellees.

J. HOWARD MCGRATH, Attorney General of the United States, as successor to James E. Markham, former Alien Property Custodian,

Appellee,

vs.

STERLING CARR, Trustee of the Estate of Nippon Yusen Kaisya, a corporation, bankrupt,

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(Consolidated)

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Appellee.

Appellant's Reply to Briefs of Appellees

Appeal from the Judgment of the United States District Court for the Northern District of California, Southern Division.

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TABLE OF AUTHORITIES CITED

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The appellees, Maurice C. Sparling, Liquidator of The Yokohama Specie Bank, Ltd. of San Francisco, and J. Howard McGrath, Attorney General, have each individ-

ually submitted a reply brief. With the Court's indulgence we shall answer both briefs in one. In doing so we desire to call the Court's attention that in our opinion there are in appellees' brief many inaccuracies in statements of fact, but we shall refrain from particularizing such instances and shall approach both briefs from the overall standpoint, feeling confident that this Court is fully cognizant of all of the evidence and its implications and inferences.

In both briefs three points are urged: (1) That the evidence is sufficient to sustain the decision of the lower court, (2) that plaintiff is barred by illegality, and (3) the *Propper* case is conclusive on the subject. We shall address ourselves to the above subjects in order.

I.

THAT THE EVIDENCE IS SUFFICIENT TO SUSTAIN THE DECISION OF THE LOWER COURT

In support of the position of appellees numerous cases are cited pertaining to the law on appeals. We need not refer to the same and in fact have no criticism of these authorities, but we do protest against the conclusions drawn from the application of law therein to the facts of this case. It has been the position of the trustee in bankruptcy before the lower court that there is no evidence from which the court could come to any conclusion other than that the total consideration was advanced by the NYK and is presently in the Yoshio Muto Special Account; that as a result, under the law of the State of California, a resulting trust is imposed by equity in favor of the individual furnishing the consideration. In this instance the Trustee in bankruptcy herein stands in even a more equitable position than the old NYK. He represents all of the American creditors of

the NYK and is being opposed by the Office of Alien Property solely on the ground that the Office of Alien Property has vested itself of the funds of the Empire of Japan. However, such vesting is subject to any proved and valid claim which impresses a trust in favor of any and all such American claimants against the Empire of Japan, among whom the claimants in this bankruptcy would be included. However, the trustee of the NYK represents a particular group of claimants—creditors of the NYK specifically.

We are intentionally not referring to Maurice C. Sparling, the Liquidator of The Yokohama Specie Bank, the other appellee, because in truth and in fact he is only a stakeholder and thus should have no personal interest in the subject matter.

Before the lower court counsel for appellant constantly urged that the evidence in the case must be viewed from an overall perspective, taking into consideration the background consisting of the imminence of war, the urgency for the repatriation of the Japanese, the desire of the American Government to have the Japanese return to Japan, and the necessity of accomplishing such repatriation with as few legal entanglements in the United States as possible during the course of its execution. Of necessity, in accomplishing this, the requisitioning of the Tatsuta Maru would have to be factual and all of the supporting instruments would have to lend credence to the reality of such plan. For the Court to ignore the underlying plan, to refuse to view evidence presented in the light of the incidents of the year 1941, and to take the position that it will look only to the formal affidavits prescribed by the Treasury Department of the United States as contradictory

to the whole evidence before the Court, particularly at a time when the United States Treasury Department had full knowledge of the reason, the plan, the basis and the method of the repatriation operation, is the grave error of which the trustee in bankruptcy is complaining. We submit that the trial court was in error when it gave any weight to affidavits filed by the NYK or Yoshio Muto as contradictory evidence, particularly when it is obvious that the plan was formulated in accord with diplomatic policy and necessity of the time. In order to carry out the plan it became necessary to have these affidavits in the form in which they were then made. To have the trustee in bankruptcy, who represents American NYK creditors, thwarted in his attempt to secure this money rightfully due the individual creditors of the NYK, as against the Office of Alien Property representing all creditors of the Japanese Government, and which stands in no stronger position than the Japanese Government, is, we submit, indeed an error, and amounts to a travesty of justice towards the creditors of the NYK in the United States.

Counsel for appellant is fully aware that if this Honorable Court refuses to view all of the evidence as a whole, i.e., as part and parcel of one master plan, including the affidavits pertaining to the execution thereof, giving each portion its proper weight and place, we must bow to the authorities which sustain the contention of the appellees.

Incidentally, counsel for both appellees have made great ado about the weakness of the evidence, and we desire to call the Court's attention to the fact that first of all, due to the intervention of the war, it was impossible to secure any evidence until the year 1947 at the earliest. Certainly the

evidence presented as to the negotiations between NYK Tokyo and the Japanese Government in 1942 gives a clear and distinct portrayal of the acts of the parties in 1941 and 1942. It also gives to this Honorable Court the only factual basis upon which the law of the State of California can impose a resulting trust, to wit, actual consideration delivered to the Muto Special Account in the United States by the NYK through the device of the Japanese Government and Consular channels, with NYK receiving no consideration whatever in return. The Trustee herein, as the plaintiff, has come into court asserting legal rights to this fund, not representing the NYK but representing the American creditors of the NYK. We submit that from all of the evidence before this Court, the Court should conclude that the lower court was in error in failing to make a finding, first, that consideration was forthcoming from the NYK; second, that appellant carried the burden of proof and showed a general plan incidental to which money was advanced, which money according to law now is rightfully the property of the creditors of NYK as against general creditors of Japan; third, that the affidavits and applications submitted by appellees must be given no more than their due weight as part and parcel of an overall plan to repatriate Japanese nationals, and not as conclusive admissions against interest by appellant.

We submit that this Honorable Court in considering all of the evidence before it should analyze the same in the same manner as if appellees were the Empire of Japan. In such a case the testimony introduced by appellant, to wit, documents of the Empire of Japan setting forth the arrangement with NYK Tokyo, including all of the plans

and the agreements to repay, would not be adjudged as of such weak character as claimed by counsel, but would be considered as strong and conclusive of the facts. In fact it would be so strong that it should be considered as conclusive admissions against interest of the Empire of Japan, sufficient to deprive the Empire of any standing in such action. In such a proceeding certainly the American creditors would have the right to look to this fund, which arose out of consideration furnished by the NYK in Tokyo and by it delivered to the Empire of Japan for a special purpose. Why appellees should be accorded any greater rights in a resulting trust action, the basis of which is consideration furnished, than creditors who look to such consideration, is a question to which the lower court has been oblivious.

It is necessary in examining this case to strip it of all legal technicalities and complications, for only when that is done can one perceive clearly the true relative positions of the parties involved. Counsel for appellee McGrath urge that the rights of the Office of Alien Property have intervened. What rights have intervened? The only rights that have intervened are the rights of the American creditors of the Empire of Japan, including the NYK creditors. Under Alien Property vesting orders, the Office of Alien Property succeeds only to such rights as the alien had. In this case we submit that the alien Empire of Japan had no right to this fund since it has so admitted in writing on numerous occasions over the period of seven years commencing with 1942. We maintain that there can be no other conclusion than that the lower court has committed error in finding that appellant has not carried the burden of proof.

merely because certain evidence, *contradictory on the surface,* has been admitted. This purported contradictory evidence, if the action were between the two original parties, viz., the NYK and the Empire of Japan, would certainly not be considered as admissions in writing against the moving party. Any such attempt would be completely disposed of by the actual correspondence between the original parties setting forth the whole plan, including the necessity of supplying to the Treasury Department the necessary applications, which in reality are contradictory to the actual facts; that the present trustee in bankruptcy should be met with such a bar and the American creditors thereby be deprived of their rights, is grave error committed by the lower court.

II.

THAT PLAINTIFF IS BARRED BY ILLEGALITY

The second point no doubt will be considered only if the Court is of the opinion that there is merit to appellant's contention that the lower court has committed error in holding that appellant has not convincingly met the test necessary to establish a resulting trust.

Counsel for appellees have urged that the evidence presents a plan where both parties, the Empire of Japan and the NYK, were in pari delicto in attempting to bring NYK money into the United States in a manner which would prevent creditors from reaching it. This, they assert, is a fraud and the courts should afford neither party a remedy. Counsel then argue that since appellant stands in the shoes of NYK and the Office of Alien Property stands in the shoes of the Empire of Japan, and since both were in pari delicto, the court would not afford its process in aid of such fraud.

The weakness of such conclusion is obvious when we realize that the appellant before the lower court was the trustee in bankruptcy, representing the American creditors of NYK, and one who has the right and the duty to seek such assets of the NYK as can be found within the jurisdiction. In such circumstances a trustee in bankruptcy stands in a much stronger position than his predecessor. In such cases the courts do not *aid* a fraud but in reality *undo* a fraud—in the instant case by making available to the creditors the consideration which is rightfully the funds of the NYK under the California resulting trust law. Accordingly, under elementary law, even if there were illegality in the transaction as claimed by appellees, such illegality would not be a bar to a recovery by a trustee in bankruptcy.

Remington on Bankruptcy, Vol. 2, Div. 8, Sec. 1126

> "But they (trustees) do not merely stand in the shoes of the bankrupt. They are vested as to property in the possession of the court with the rights of a creditor holding a lien thereon by legal proceedings, and as to other property with the rights of a judgment creditor holding an execution duly returned unsatisfied."

The law is generally well settled that the question of pari delicto of a defendant (or a predecessor of the trustee in bankruptcy) has no application and cannot be raised against an action of a receiver or a trustee in bankruptcy who represents the creditors and the Court in the administration of the assets. No longer is the bankrupt in existence. The NYK as an entity has vanished. This rule of law is an exception to the ordinary rule and allows the trustee or receiver to attack any transaction as if there were no conspiracy or pari delicto relationship existing between the

former parties. Recovery is allowed in favor of the trustee on the basis of public policy.

In

Camerer v. Calif. Savings & Commercial Bank, 4 Cal. 2d, 159, at 170

it is stated:

"It is fundamental that a liquidating receiver represents the interests of depositors and creditors. It is equally fundamental that as a general rule, the receiver takes the insolvent's property subject to all liens, defenses and equities to which it is subject in the hands of the insolvent, and that he administers on behalf of creditors no greater title or estate than the debtor had. (Citing authorities.) *Without denying the validity of this general rule, there are certain situations where the receiver is permitted to assert rights and defenses not available to the insolvent. Thus, it is held that although the insolvent debtor cannot set aside a transfer in fraud of his creditors, as he is in pari delicto, the receiver acting for the creditors may attack it.* (See 23 R.C.L., p. 116, citing cases.) It is also held that although an unrecorded conveyance or mortgage is valid as against the grantor or mortgagor, his receiver prevails over the holder under the unrecorded instrument under statutes which provide that unrecorded transfers are void as to creditors. (Citing authorities.) The justice and equity of such exceptions to the general rule that the receiver has only the rights of the insolvent debtor are apparent." (Italics added.)

Bank of Orland v. Harlan, 188 Cal. 413;

First National Bank of Reedley v. Reed, 198 Cal. 252;

Wood v. Kennedy, 117 Cal. App. 53.

The whole transaction is similar to the class of cases where recoveries are allowed for the return of money where transactions are entered into for the purchase of corporate stock which has been issued without a permit. In those cases, because of public policy, the courts refuse to entertain a defense of illegality of purchase and allow recoveries. The case at bar is in principle identical. Public policy will resist any attempt of appellees to urge pari delicto, inasmuch as they can be in no better position that their predecessor the Empire of Japan.

Hansen v. California Bank, 17 Cal. App.2d, 81, at 96;
Kahle v. Stevens, 214 Cal. 89, at 93;
Deane v. Shingle, 98 Cal. 652.

But irrespective of the legal question as to whether the trustee in bankruptcy is subject to the illegality bar, we maintain that no fraud or illegality exists in the case at bar. Certainly, *where no creditors' rights are involved,* a resulting trust cannot arise as between two parties in a situation where both parties are participants in a fraud. But where is there any fraud by anyone in this case? All we find is an agreement between the United States Government and the Japanese Government to conform to all the laws and regulations of the United States; it is an arrangement whereby the NYK is merely an "individual" who supplies the consideration requested by the Empire of Japan, with the understanding that the consideration and the results of such consideration are to remain the property of the NYK. The NYK had no fraud in mind when entering into this agreement to enable its vessels to enter the United States; the NYK had no thought of bringing money into the United States contrary to Treasury Department license provisions.

The arrangement was made between the two governments, and under this arrangement the money was actually brought into the United States under a license in favor of Muto. All of the passenger fares were then deposited in the Muto account under a license. Therefore, up to this point there was no illegality in the transfer of the money to the United States, or in its remaining here in the account of Muto. The money once here legally remains here legally.

Under these circumstances certainly there can be no question of fraud or evasion of any existing laws. Certainly not against the creditors of the NYK. If any fraud was perpetrated, it was perpetrated *against* the creditors of the NYK in the United States, and as to such creditors the Office of Alien Property, standing in the position of the Empire of Japan, would have no right to urge such fraud. Indeed the creditors of the NYK were hindered by the agreed action of both governments in bringing this vessel to the United States. Under these circumstances it is absurd for counsel to present to this Court any contention of fraud or unlawful conduct in an attempt to bar the rights of the American creditors. If anyone should be barred from asserting such a claim, even if there were any basis for it, it would be the Office of Alien Property as successor to the Empire of Japan.

The only legal issue before the Court is the right of the Office of Alien Property standing in the shoes of the Empire of Japan, and the right of appellant, representing the American creditors of NYK, to this particular fund, which came into the United States legally in accordance with all of the licenses, provisions, rules and regulations, and is still here in the possession of the United States under such rules and regulations.

Counsel for appellees on this subject of illegality urge that as a matter of law the District Court may not give judicial recognition to appellant's claim that the NYK had a beneficial interest in the Counsel's Special Account. The obvious error of counsel is in presuming that we claim that the NYK has a beneficial interest, as such term is used, in the funds transferred to the United States in the case at bar and in the proceeds of passage hire deposited to the account in question. Further, the conclusion of illegality is arrived at by assuming that these acts which resulted in the fund, were done primarily for the benefit of the NYK. We emphatically oppose such an original premise and the conclusions which are drawn therefrom. We submit that the NYK funds in trust which we are presently seeking, only became such by the operation of California law, and that the so-called "beneficial trust" held for the NYK and which the trustee is seeking to obtain for NYK creditors, is one which came into being only after an interpretation of all of the acts of the parties; we have never contended that the original parties claim that there is a beneficial trust.

We respectfully submit that a strict application of technical rules based on the camouflage entered into by the Empire of Japan and the NYK and tacitly approved by this government, should not prevent the American creditors from the exercise of their rights based on the true facts, especially where the American creditors of NYK played no part in such camouflage.

III.

THE PROPPER CASE, REPRESENTED AS BEING CONCLUSIVE

Appellant in his opening brief has gone into this subject thoroughly and any lengthy reply to the answer of appellees would be unduly burdening the Court. The distinction between the contentions of appellant and appellees is obvious. Appellant asserts that the *Propper* case gives the Court the right to litigate the rights and liabilities of the trustee in bankruptcy and the Office of Alien Property in connection with the fund in question. Appellees totally disregard this intermediate step and look to the ultimate result of such litigation and contend that if the litigation is successful, there would be a recognition of a transfer of credit.

We do not agree with counsel's statement that we claim at the time the funds were transferred to San Francisco and deposited in the Muto Special Account, the NYK was the beneficiary of an interest in such funds. It is immaterial what the position of the NYK would have been, had no bankruptcy proceeding intervened. Appellant, the trustee in bankruptcy, now asserts a claim based upon the law relative to resulting trusts, including the right to apply to a court for a determination in favor of the creditors of the NYK. That is very far afield from a claim that it was the actual intent of the parties to transfer a beneficial interest along with the funds. The transfer of the funds was legal and was approved by the Treasury Department in favor of the Japanese Consul. Only at the present date we are asking the Court to determine that under California law the creditors of NYK in the United States have a superior right to the funds in question, which legally entered the United States as a licensed transfer.

The recent case of

State of The Netherlands v. Federal Reserve Bank (1951), 99 Fed. Supp. 655

throws considerable light upon the question of whether the *Propper* case is controlling in all instances. It is an action by State of The Netherlands for recovery of certain bonds which were in possession of the United States Federal Reserve Bank, having been deposited by one Archimedes, an interpleaded defendant, the issue was decided on other phases, but is referred to here because the plaintiff therein urged that the *Propper* case was conclusive as against any transfer to the defendant Archimedes by interpleader. The Court exhaustively considered the recent Supreme Court decisions in *Propper v. Clark,* 1949, 337 U.S. 472; 69 S.Ct. 1333; 93 L.Ed. 1480, and *Lyon v. Singer,* 1950, 339 U.S. 841; 70 S.Ct. 903, 94 L.Ed. 1323, and distinguished them in a manner similar to Appellant's claim of the inapplicability of the *Propper* case to the facts in the case at bar. On page 666 the Court stated in this regard:

> "In examining these cases, an explanation of their different results can be found which is also in keeping with the purpose of the regulations in question. In both the Bernstein and Propper cases, the courts had under consideration the extent of interests derived from transactions which were, in themselves, proscribed. In each, the purported transfer, which would give rise to the claim, was illegal. On the other hand, in Lyon v. Singer the rights which were validated arose out of transactions not illegal in their inception. In one case a credit was transferred before the freezing order was applicable; in another, a draft was purchased in a foreign country though drawn on and payable by a bank

located in New York. In these instances, it was only the payment of the credits which the federal regulations interdicted and not the underlying transactions that gave rise to the claims. Under such circumstances, the Supreme Court permitted the recognition of the validity of the claims.

"From the reasoning in these cases, it would seem to follow that inasmuch as the actual transaction through which Archimedes asserts his interest was, by law, prohibited, he cannot avail himself of the Lyon v. Singer rule. Accordingly, I do not think that he has any valid claim to the bonds. But, in this conclusion, realizing that it emanates from a distinction which the Supreme Court did not itself express, there may be some doubt about it. For this reason, *it is desirable that the applicability of the freezing orders be, at this point, disregarded* so that the nature of Archimedes' interest in the bonds may be evaluated *as if the monetary regulations do not dispose of the issue.*"

However, as emphatically stated in our opening brief, a decision by this Court in favor of appellant would result in no transfer; appellant concedes that in the event of an affirmative decision it would still be necessary to apply for the consent to transfer the money that is required under Treasury Department licensing regulations. That we are prepared to do. We do take issue with the conclusion that the *Propper* case precludes the right of appellant to litigate the subject matter on the basis that the end result would be a transfer of credit without a proper license having been procured. With a determination by this Court that these funds rightfully belong to the American creditors of the NYK, appellant would be in a position to take the

next logical step, viz., to apply for a license to effect the transfer. Appellant expressly urges that the *Propper* case allows the court to litigate the rights between the parties provided that any transfer of credit must comply with licensing requirements. We emphasize the fact that the Court is only requested to make its finding that appellant has superior rights to these funds; it is fully understood that in the event such finding is made, it would still be impossible for appellant to transfer title to the money unless licensed so to do by the Treasury Department.

In conclusion appellant submits that the judgment of the District Court was in error and should be reversed.

Respectfully submitted,

Louis J. Glicksberg

Attorney for Appellant.